



Bundesverband Investment
und Asset Management e.V.

Mr. Carlo Comporti
Secretary General

CESR the Committee of European
Securities Regulators
11-13 avenue de Friedland
75008 Paris
FRANCE

Contact:

Dr. Magdalena Kuper
Phone: +49.69.154090.
Fax: +49.69.154090.
Magdalena.Kuper@bvi.de

20 August 2008

Call for Evidence on the request for advice to CESR on the UCITS asset management company passport

Dear Mr. Comporti,

BVI¹ greatly appreciates the opportunity to present its views on possible structure and principles in terms of the UCITS management company passport and respective amendments to the UCITS Directive. Given the very tight timeframe for the requested advice to the Commission, we would like to thank CESR for consulting the industry at this early stage of deliberations. To facilitate proper and viable solutions, we are convinced that this close exchange of views should be continued throughout the work of CESR.

Preliminary remarks

BVI strongly supports the notion of vesting UCITS management companies with an EU passport enabling them to operate cross-border on the basis of freedom of services. As already expressed on previous occasions, we consider the management company passport a logical and necessary element of integration in the EU market for investment funds. EU passport for management companies would allow for exploiting economies of scale and utilizing centres of excellence by concentrated execution of management and administrative functions with ultimate cost savings to the benefit of investors. Moreover, it is capable of enhancing competition by

Director General:
Stefan Seip
Managing Director:
Rüdiger H. Päsler
Rudolf Siebel

¹ BVI Bundesverband Investment und Asset Management e.V. represents the interest of the German investment fund and asset management industry. Its 89 members manage currently assets in excess of EUR 1.6 trillion both in mutual funds and mandates. For more information, please visit www.bvi.de.

Eschenheimer Anlage 28
D-60318 Frankfurt am Main
Postfach 10 04 37
D-60004 Frankfurt am Main
Phone: +49.69.154090.0
Fax: +49.69.5971406
info@bvi.de
www.bvi.de



enabling middle-sized fund managers, not only those belonging to international groups, to enter national markets with products suiting preferences of local investors.

We acknowledge that realization of the company passport idea is a complex task which might need new and innovative solutions in order to meet the standards of the UCITS Directive. However, we are convinced that the concerns brought forward by some with regard to the effectiveness of supervision and investor protection can be overcome by reasonable efforts both on regulators and industry side.

Indeed, we think that the industry has a vital role to play in accommodating the management company passport in practice. Thus, our following suggestions refer to a few cases in which the industry's commitments towards the fund supervisor might go beyond the level currently required by the UCITS Directive. These concessions are meant to mitigate concerns in terms of effective supervision and to enhance acceptance of the passport among competent authorities.

On the other hand, the proper functioning of the passport will depend to a great extent on the attitude of national authorities bearing responsibility for fund supervision. The power to authorise UCITS gives the competent supervisor a sharp instrument which is necessary in order to verify compliance with the applicable legal regime, but which might also be abused in order to inhibit authorisation of cross-border managed funds on grounds of alleged shortcomings. Therefore, the UCITS Directive should be very clear on reasons for which the authorisation of UCITS managed via the company passport might legitimately be refused.

Specific comments

Our views on the possible regulatory approach to the management company passport (MCP) set out in following focus on the four main areas for action identified by CESR in the background to the Call for Evidence. Questions raised by the Commission in its request for advice are accounted for in the relevant context.

1. Clear and systematic allocation of regulatory responsibilities

In our opinion, a clear division of responsibilities between the authorities responsible for the management company ("home State regulator") and the UCITS ("host State regulator") is key to the successful functioning of the MCP. In a first move, however, requirements of the UCITS Directive should be thoroughly split in those applicable to the management company (MC) and those relevant to the fund or its depositary. On this basis, the allocation of duties to the competent authorities should be basically self-explanatory.

After a first scrutiny of the revised draft directive presented by the Commission, the following picture can be drawn:

- Rules pertaining to the management company:
 - o Articles 6-8: fit and proper test, capital requirements
 - o Article 11: qualified holdings
 - o Article 12: organisational requirements for MC, including some aspects of risk management and record keeping
 - o Article 13: conditions for outsourcing
 - o Article 14: code of conduct principles, to be specified at national level
 - o Article 51 (1): limits on acquisition of voting rights
 - o Articles 78 (1), 83, 84: general restrictions on lending, borrowing and short sales in terms of UCITS management
- Provisions relating to UCITS:
 - o Article 5: conditions for authorisation (for externally managed investment companies, additional standards laid down in Articles 24 to 26 apply)
 - o Articles 45-52: rules on investment policies, including risk management processes to measure the risk profile of UCITS portfolio
 - o Articles 63-77: investor information, including auditing of the UCITS annual report
 - o Articles 78-85: terms for subscription/redemption, valuation, NAV calculation, treatment of income; restrictions on lending, borrowing and short sales
 - o Articles 86-91: cross-border marketing within the EU
- Obligations regarding the depositary are stipulated in Articles 29-33

A cross-check against Annex II of the UCITS Directive listing activities of collective portfolio management shows that nearly all functions, except for monitoring of regulatory compliance and record keeping which are entrusted to the MC under Article 12 (1), are attributable to the UCITS and should be performed in accordance with the laws and regulations of the host Member State. The host State regulatory competences must not, however, include organisational backing of the fund management which should be applied consistently on the basis of the MC home State regime. Allocation of the function “customer inquiries” seems unclear, but due to its organisational implications, we would tend to vest it in the MC rather than UCITS. As regards risk management, the UCITS Directive provides for a split of responsibilities: rules for personal transactions, dealing on own account and monitoring of compliance with investment principles and limits are to be implemented at the level of MC under Article 12 (1), whereas the

measurement of specific portfolio risks is closely linked with the UCITS and should be conducted under the law of the host Member State.

Functions attributable to the MC should comply with the legal regime of the home Member State. In contrast, the remits of UCITS should be governed by the laws and regulations of the host Member State meaning the country in which the UCITS has been authorised and which should be deemed the place of its domicile. This new approach should be reflected in Article 4 of the draft UCITS Directive.

Consequently, the supervision of the MC related tasks should be conducted by the home State authority. The host State supervisor situated in the home Member State of the UCITS would then be responsible for overseeing management functions assigned to the fund.

As regards the depositary, it should be registered or at least established in the home Member State of the UCITS and subject to the supervision of competent authorities of that Member State. Article 20 (1) of the draft UCITS Directive should be amended to that effect.

2. Necessary means to verify, monitor and enforce regulatory requirements

The novelties in conduct of supervision relating to the MCP are limited to the supervision of UCITS managed cross-border. In this regard, effective supervisory mechanisms are either already existent or can be introduced by slight amendments of supervisory practices / EU provisions:

- **Verification of compliance with the host State rules**

The host State authorities responsible for fund supervision will remain competent to grant authorisation to the UCITS. The sole control over the UCITS authorisation gives the host State authorities significant powers which should be used in order to verify the initial compliance of the fund with relevant provisions.

In the context of authorisation, UCITS supervisor should be entitled to request information on the MC in order to assess its ability to manage the UCITS in accordance with laws and regulations of its domicile. This additional information should pertain in particular to the employment of qualified personnel, potential outsourcing solutions, arrangements for portfolio risk management, valuation of assets and NAV calculation. It could be submitted by the MC via an extended programme of operations under Article 17 (1) or on the first occasion of authorising a UCITS in a given Member State, and should be referable to in further cases.

Notwithstanding these enhanced rights to obtain information on the MC, **the EU management company passport should be respected in any circumstances.** Only where the MCP does not embrace the whole range of UCITS management activities because the MC authorisation has been limited to certain types of products, authorisation of UCITS falling beyond the licensed categories might be refused. The potential of host State authorities to undermine functioning of the MCP in the UCITS authorisation process should be mitigated by appropriate provisions at EU level (e.g. clarification in Article 5 that authorisation of UCITS managed cross-border may be refused only on grounds of failure to comply with the requirements of the Directive / implementing national law or due to insufficient scope of the MCP).

- **Monitoring of compliance on ongoing basis**

The ongoing supervision of UCITS pertains in particular to the correct calculation of NAV, valuation of assets, adherence to investment and risk management limits, unit subscriptions and redemptions. In this regard, the competent authorities should have permanent access to the complete accounting data of the fund, including any relating analyses and parameters. This information could be transmitted to the fund supervisor on a daily basis or held available at the supervisor's request by the depositary. When determining the appropriate means of access to information, the operating and cost implications for the affected entity should be taken into account.

Information of the fund supervisor should be complemented by the regular auditor reports on the UCITS. In order to warrant comprehensive supply of data relevant to the fulfilment of auditing duties, fund auditor might be required to enter into an information sharing agreement with the auditor of the MC as proposed in the context of master-feeder structures under Article 57 (1) of the draft UCITS Directive.

- **Effective enforcement mechanisms**

The right to withdraw authorisation of UCITS puts the fund supervisor in a very strong position in terms of enforcing lawful conduct on the part of the MC. Formal enforcement tools below the level of withdrawal are provided for in Article 93 (2), especially in subsections e), i) and j) of the revised draft directive. In the context of cross-border management of UCITS, these powers can be exercised by the UCITS supervisor either on its own or in cooperation with the MC home State authorities according to the procedure laid down in Article 18 (3) to (8). In order to foster effective fund supervision, the MC home State supervisor should not be entitled to challenge the reasonability of measures meant to enforce fund related rules of another Member State.

On these grounds, we are convinced that effective supervision of cross-border management activities can be ensured in a relatively easy manner by a few adjustments to the existing UCITS supervisory regime. Extensive information rights and enforcement mechanisms warrant a strong position of the fund supervisor and uncompromised protection of investors. In any case, there is no demonstrable need in terms of the effectiveness of supervision to require performance of selected management tasks in the UCITS home Member State.

3. Cooperation duties of supervisory authorities

In our opinion, obligations incumbent on competent authorities to furnish information and other assistance to partner authorities are already set out in commensurate way in the revised draft of the UCITS Directive.

As regards communication between national authorities, Article 96 (2) provides for unsolicited supply of information required for the purpose of carrying out supervisory duties. Concerning the management of UCITS under the MCP, this duty should cover any information with potential impact on fund administration or conduct of business of the MC respectively. Further information on the MC may be requested pursuant to Article 104 (1) or in accordance with the procedures for exchange of information to be adopted by the Commission under Article 100.

In addition, Article 96 (3) of the draft UCITS Directive confers upon the fund supervisor the right to request the cooperation of the MC home State authorities for on-the-spot verifications and investigations on the territory of the latter. The request shall be met by the MC home State authorities carrying out the requested procedure itself, allowing the fund supervisor to take the necessary steps or vesting the task with qualified third parties. In the first case, the UCITS supervisor is entitled to delegate members of its own personnel to accompany the investigation / verification process.

Potential problems in terms of information exchange or joint investigation / verification shall be brought to the attention of CESR. In these circumstances, it appears advisable to apply the mediation mechanism adopted by CESR as informal tool of dispute resolution. The use of mediation should be envisaged also in relation to infringements of the cooperative enforcement procedure pursuant to Article 18 (3) to (8). However, in order to provide for reliable solutions, participation in the supervisory mediation should be declared mandatory and at least a "comply or explain" approach should apply to mediation results.

4. Conditions for effective enforcement actions for relevant entities

The regulatory regime described above provides for an effective set of tools to enforce supervisory measures. As regards MC and UCITS depositary, supervisory enforcement under the MCP bears no difference compared to purely national situations. The same applies for corporate type funds established as legal entities in their respective domiciles.

In case of contractual UCITS which lack legal personality, supervisory decisions in terms of fund management are aimed at the MC. Enforcement of such measures against MCs operating cross-border might encounter certain difficulties if conducted in national context, e.g. under Article 18 (3), (5) or (6). Therefore, MCs of contractual funds might be required to retain a limited local representation in the home Member State of the UCITS. The local representation should act as a contact point for information requests or any other communications on the part of fund supervisor and be nominated addressee for supervisory measures taken in relation to the UCITS. It should, however, not be required to have the legal status of a branch in order to keep the operating expenses for the MC at a minimum. Moreover, the MC representation must on no account be under the duty to perform certain management functions in relation to cross-border managed funds.

Rules pertaining to the MC local representation, if any, should be laid down exclusively at EU level in order to discourage protectionist practices and to warrant smooth functioning of the MCP.

We hope that our suggestions will help CESR to devise a viable concept for the realization of the MCP. We would like to assure CESR of our willingness to provide continuing assistance and to engage in further discussions on the subject at hand.

Yours sincerely

BVI Bundesverband Investment und Asset Management e.V.

Signed:
Stefan Seip

Signed:
Dr. Magdalena Kuper